

RESERVE BANK OF FIJI

QUARTERLY REVIEW

June 2007

Private Mail Bag, Suva, Fiji Islands
Telephone: (679) 331 3611, Facsimile: (679) 330 1688, E-mail: rbf@reservebank.gov.fj
website: <http://www.reservebank.gov.fj>

QUARTERLY REVIEW OF THE ECONOMY & FINANCIAL CONDITIONS

Overview	3
The International Economy	5
International Economic Conditions	5
International Financial Markets	9
The Domestic Economy	12
Domestic Economic Conditions	12
Consumer Spending	12
Production	12
Public Finance	15
Inflation	16
Labour Market	17
The External Sector	18
Domestic Financial Conditions	18
Money Markets	18
Capital Markets	19
Foreign Exchange Markets	19
Financial Intermediaries	20
Banking Industry Quarterly Condition Report - March 2007	21
Insurance Industry Quarterly Condition Report - December 2006	31
For the Record	
<i>Beware of Scams - Advance Fee Fraud & Lottery Scams</i>	34
<i>World Bank Releases its Report on Fiji's Framework for Combating Money Laundering and Terrorist Financing</i>	36
<i>Reserve Bank Board Leaves Monetary Policy Unchanged</i>	37
Statistical Annex	38
Reserve Bank of Fiji Publications	40

OVERVIEW

Global economic conditions remained buoyant in the June quarter despite a slowing United States (US) economy. China remains a substantive contributor to world growth while encouraging performances were noted for our other major trading partners driven largely by business investment.

The International Monetary Fund (IMF) estimates that the world economy will expand by 4.9 percent this year, following a 5.4 percent growth in 2006. Downside risks to this assessment include a prolonged US housing market slowdown and inflation pressures emanating from crude oil prices.

Globally, monetary policy was mainly on a tightening bias with New Zealand and the Euro-zone raising interest rates over the quarter.

The growth outlook for most of our major trading partners is optimistic with only US economic growth projected to slow.

In the international financial markets, global equity markets rallied, while bond markets were generally weaker. On exchange rates, with the exception of the Yen, the US dollar generally weakened against Fiji's other major trading partner currencies.

Locally, revised growth estimates provisionally indicate the economy expanded by 3.6 percent in 2006. The following sectors were expected to have led growth: finance, insurance, real estate & business services; wholesale & retail trade, restaurants & hotels; manufacturing; building & construction; community,

social & related services and electricity & water.

For 2007, a 3.1 percent economic decline is forecast largely as a result of lower Government spending and a contraction in restaurants & hotels, building & construction, and wholesale & retail trade sectors.

Various indicators available to date have largely confirmed a slowdown of overall economic activity.

Despite buoyant data on household incomes, partial indicators of consumer spending including consumption lending and currency in circulation slowed in the year to June while net Value Added Tax (VAT) collections for the same period registered a decline of around 8.4 percent over the 2006 corresponding period.

Production in the fisheries and timber industries performed well. Sugar crushing began on schedule in June but was affected by low cane supply and operational and plant problems.

Performances of other sectors including garments and copra were weak while the electricity sector grew only marginally. Furthermore, the absence of gold mining has placed further constraints on overall output.

The **tourism** industry remained subdued in the June quarter, resulting in an overall reduction in flights by the national carrier Air Pacific Limited. Visitor arrivals in the first half of the year fell by 5.1 percent. Hoteliers are more severely affected than the arrivals numbers suggest as the

numbers include arrivals of visiting friends and relatives, who are less inclined to utilise the local hotels.

Investment levels are weak, in line with the slowing building and construction sector as various large projects are completed and others have stalled. Consequently, imports of investment type goods and lending for investment purposes have also slowed.

Inflation rose substantially during the quarter. The headline measure was 7.1 percent in June, while the underlying measure - the trimmed mean - was 3.2 percent. Supply shocks, both domestically and externally have led to exorbitant food prices in recent months. The year-end inflation forecast has been revised to around 7.0 percent

Employment conditions in some sectors continue to be weak due to the prevailing economic contraction. The slowdown in the tourism industry, the closure of Emperor Gold Mining Company Limited and various construction projects being on-hold are contributing factors.

On Government's fiscal stance, cash flow data indicated that cumulative to March, Government recorded a net surplus of \$15.0 million, equivalent 0.3 percent of GDP. The fiscal outturn was underpinned by a 0.4 percent decline in expenditure

payments, which in absolute terms, outweighed the 11.1 percent decline in revenue collections (excluding asset sales).

Export earnings improved while import payments declined in the first five months of 2007 when compared to the similar period a year ago. However, the trade gap at \$667 million continues to be of concern.

Foreign reserves at the end of June were around \$859.9 million (provisional), sufficient to cover 3.5 months of import payments of goods.

In May 2007, the Bank lowered the Statutory Reserve Requirement (SRD) for commercial banks from 7 percent to 6 percent and in June, exchange control approval processes for advance import payments were relaxed.

The impact of the credit ceiling which was implemented on 6 December 2006, continued to filter through. Growth in outstanding credit of commercial banks and licensed credit institutions continued to slow. Deposit and lending rates of commercial banks have largely declined reflecting improved liquidity conditions.

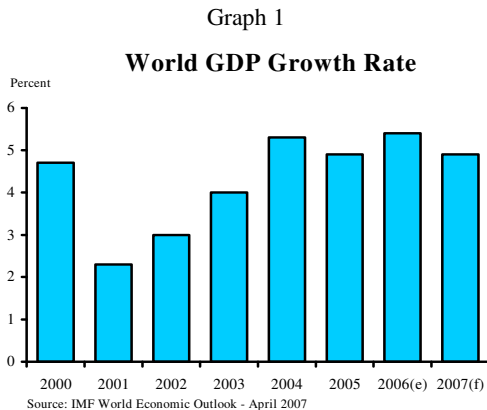
The Bank will continue to monitor developments in the economy in the coming months and align monetary policy accordingly.

THE INTERNATIONAL ECONOMY

International Economic Conditions

World economic and financial conditions continued to improve in the June quarter, with prospects of a good performance this year. This is despite a slowing US economy, which is currently experiencing a downturn in its housing sector. China continues to be the locomotive for global growth, this time greatly assisted by the Latin American and Sub-Saharan developing economies. This is in addition to the firm performance of the Japanese economy and an improved outlook for the Euro-zone relative to previous forecasts. Both these areas are heading for a period of above-trend growth.

The IMF estimates that the world economy will expand by 4.9 percent this year (Graph 1).



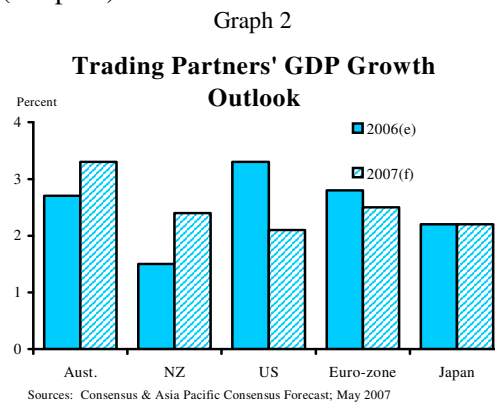
Nonetheless, there are certain factors that can undermine the current assessment. This includes the US economy deteriorating further if the housing sector weakness is prolonged. In addition, inflationary pressures could rise should crude oil prices gather momentum.

Finally, geo-political tensions could also disrupt the global growth prospects.

Monetary policy continued to be on a tightening bias during the quarter, an inevitable response to the inflationary pressures emanating from the strong economic activity, positive labour market conditions and high crude oil prices. The Euro-zone and New Zealand economies raised their key interest rates during the quarter.

Over the June quarter, global stock markets rallied while yields on bonds generally rose. On the currency front, the US dollar generally weakened against all of Fiji's major trading partner currencies with the exception of the Japanese Yen.

Economic growth of Fiji's trading partners is expected to remain strong in 2007 despite some slowing in the US and, to a lesser extent, the Euro-zone countries when compared to 2006. Australia and New Zealand, on the other hand, are expected to improve from last year. The outlook for Japan remains unchanged (Graph 2).



The **Australian** economy grew at the fastest pace in more than 3 years in the first quarter of this year, with household spending, business investment and a build-up of inventories all making substantial contributions to growth. In the three months to March, real GDP grew by 1.6 percent compared to a 1.1 percent growth in the last quarter of 2006.

Economic indicators over the current quarter are also supportive of buoyant economic growth. Employment conditions rebounded in April and kept the jobless rate at a 32-year low of 4.4 percent. This also provided an impetus for retail sales which surged in March and kept consumer confidence close to record highs in June. An index of leading economic indicators increased for the third month in April while business confidence also gained in the same month.

The Reserve Bank of Australia (RBA) kept its benchmark interest rate unchanged at a six-year high of 6.25 percent in the June quarter, after three hikes last year.

The economy is forecast to grow by 3.3 percent this year, supported by increases in household consumption, business investment and industrial production. Consumer prices are expected to ease from an estimated 3.5 percent last year, to 2.1 percent in 2007, within the RBA's target band of 2-3 percent.

New Zealand's economic growth accelerated in the first quarter as increasing interest rates drove up the currency, spurring demand for cheaper imported goods from companies and consumers. Gross domestic product increased by 1.0 percent in the March

quarter from the previous quarter when the economy expanded by 0.8 percent.

Recent indicators showed that business confidence rose in June, driven by higher dairy prices and cuts in company taxes. On the other hand, consumers may be feeling the effects of higher interest rates: retail sales fell in April, the most since February 2004 while consumer confidence fell for the second consecutive quarter in June.

The Reserve Bank of New Zealand hiked interest rates by 25 basis points to 8.0 percent in the June quarter, after housing demand and consumer spending continued to fuel inflation.

On the whole, the economy is expected to pick up this year and record a growth of 2.4 percent, driven by improvements in private consumption, investment and trade. Year-end inflation is expected at 2.2 percent this year from 3.4 percent recorded in 2006.

The **US** economy grew by 0.7 percent in the first quarter of 2007, after a 0.6 percent expansion in the last quarter of 2006. The growth was a result of a narrowing trade deficit and an increase in business spending.

Latest economic indicators were mixed. Industrial production declined in March, the trade deficit narrowed in April, consumer confidence fell in June to a 10-month low and manufacturing rose in June at the fastest pace in 14 months.

The Federal Reserve has kept the benchmark interest rate unchanged at 5.25 percent since June 2006.

The economy is expected to slow to 2.1 percent this year, largely attributed to declining business investment. Inflation is anticipated to fall from 3.2 percent last year to 2.4 percent at the end of 2007.

Economic growth in the group of **Euro-zone** countries was up by 0.6 percent in the first quarter of 2007, after a revised 0.9 percent growth in the fourth quarter of last year. The growth was attributed to a pickup in business investment.

Continuing with the encouraging economic activity in the first quarter, more recent indicators show that the Euro-region's business and consumer confidence stayed close to a six-year high in June. In addition, manufacturing growth accelerated more than expected, while investor confidence rose to a record high in June.

The favourable conditions are supported by the region's two major economies, Germany and France.

German industrial output rose the most in six months as factories increased output. In addition, the unemployment rate fell to the lowest level in 12 years in June. In France, business confidence surged to an 11-month high as employment gained.

In line with a firm economic outlook, the European Central Bank raised its benchmark interest rate by 25 basis points to 4.0 percent in June.

Growth for the Euro-zone economy is projected at 2.5 percent this year, supported by higher investment and industrial production. Year-end inflation for 2007 is forecast at 1.9 percent, compared with 2.2 percent estimated for 2006.

Japan's economic growth jumped from an annual 1.3 percent in the fourth quarter of 2006 to 3.3 percent in the first quarter of 2007. The improvement was supported by strong consumer spending and exports.

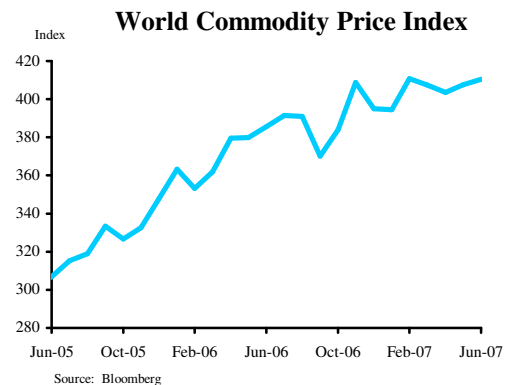
Recent data painted an encouraging picture of economic activity. Business confidence was held near a 2-year high with companies increasing their spending. Household spending rose for the fifth month, while the jobless rate remained at a 9-year low of 4.0 percent in May.

The Bank of Japan kept its benchmark interest rate at 0.5 percent in the June quarter, to ensure that strong economic growth and stable inflation is sustained.

The Japanese economy is projected to grow by 2.2 percent this year, supported by business investment. Inflation is forecast to fall marginally from an estimated 0.2 percent in 2006 to 0.1 percent in 2007.

World commodity prices rose by around 0.7 percent over the second quarter, underpinned mainly by increases in lumber, coconut oil, sugar and crude oil prices (Graph 3).

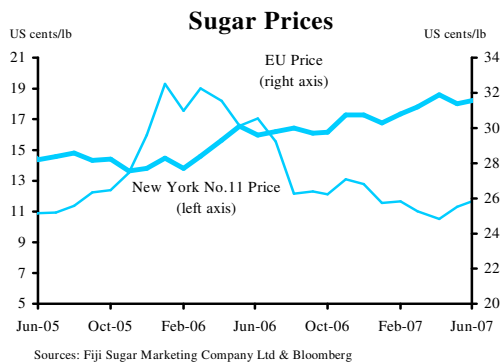
Graph 3



Against the long term declining trend, **world market sugar prices** (New York no. 11) rose by around 6.3 percent in the second quarter (Graph 4). Prices initially fell in the first month of the quarter on expectations of increased global production. However, prices later rose on speculation that Brazil would concentrate on ethanol production, an alternative source of fuel, instead of producing sugar.

Given the only very recent price hike, it may be too early to predict a change in trend. Hence prices are expected to remain low as India and Brazil increase production.

Graph 4



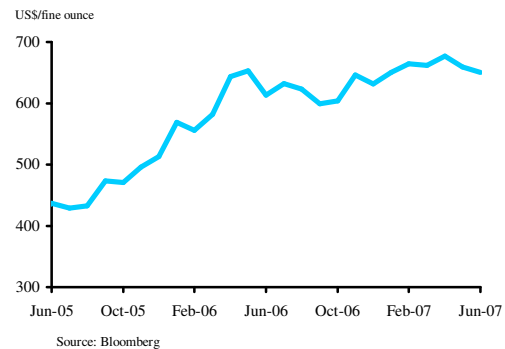
At the end of June, the European Union (EU) sugar price was around US32 cents per pound, having risen marginally over the quarter, due to a stronger Euro against the US dollar.

Gold prices declined by around 1.7 percent over the June quarter (Graph 5). Gold prices initially rose in April, after speculation that a slowing US economy will weaken the dollar. This boosted the appeal of the precious metal as an alternative investment. In addition, the on-going geo-political tensions in the Middle-East served as an advantage for

bullion.

Gold prices fell in the last two months of the quarter on speculation that the euro's rally against the dollar will stall, reducing the appeal of the precious metal as an alternative investment.

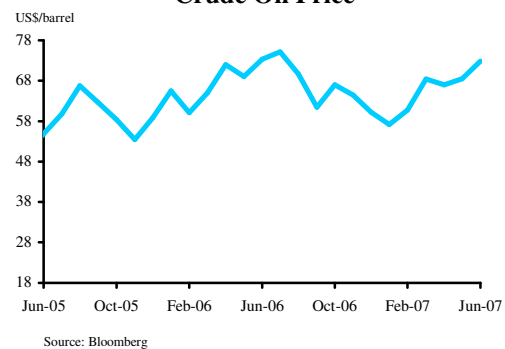
Graph 5

Gold Price

In the months ahead, gold prices are anticipated to remain high.

The **Brent crude oil price** was around US\$72.82 per barrel at the end of June, an increase of around 6.4 percent when compared to the end of March 2007 (Graph 6).

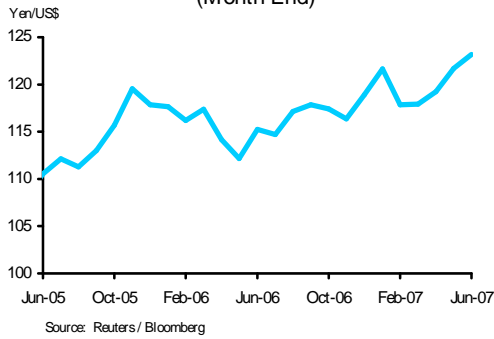
Graph 6

Crude Oil Price

Crude oil prices initially fell in April, on speculation of increased US oil

Graph 9

Exchange Rate - Yen/US\$
(Month End)

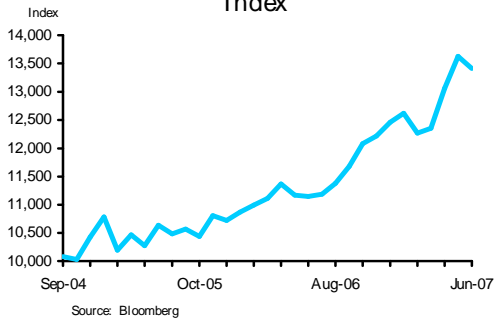


Equity prices generally rose during the three months to June, when compared to the first three months of the year.

Over the second quarter, the Dow Jones Industrial Average Index rose by 8.5 percent (Graph 10). The Dow surged in the first two months, led by aviation and energy related shares after profits surpassed estimates. However, US stocks fell marginally in June, amid concerns that the drop in consumer confidence would hamper profits.

Graph 10

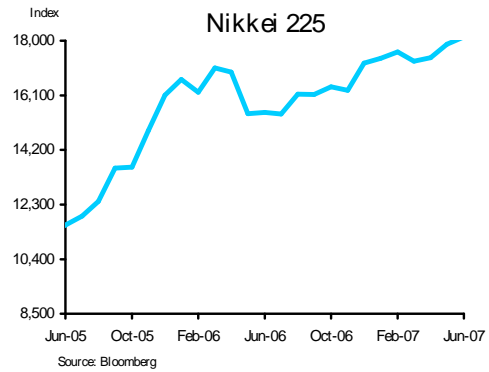
Dow Jones Industrial Average Index



The Nikkei 225 Stock Average Index rose by 4.9 percent (Graph 11) over the second quarter. The Nikkei rallied throughout the period on optimism that a weaker Yen would boost profits in export related companies.

Graph 11

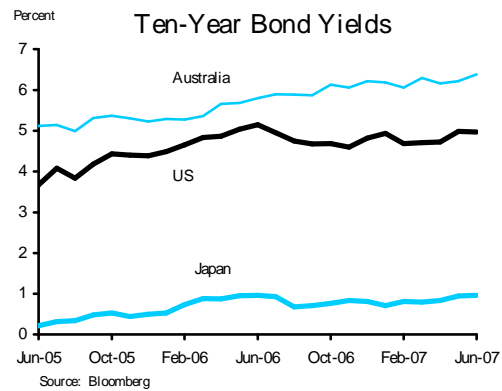
Nikkei 225



Over the June quarter, bond yields for the US, Japan and Australia all rose (Graph 12).

Graph 12

Ten-Year Bond Yields



US bond yields rose in the first two months, after a surge in stocks reduced demand for government debt

instruments. However, yields fell in June improving bond prices slightly, after expectations of negative data in the housing/real estate sector increased demand for the safety of government bonds.

Japanese bond yields rose throughout the

quarter, as the increase in Japanese stocks drew investors away from the fixed-rate return debt asset.

Australian bond yields rose in the June quarter, as stronger economic growth prompted investors to switch from bonds to other assets.

THE DOMESTIC ECONOMY

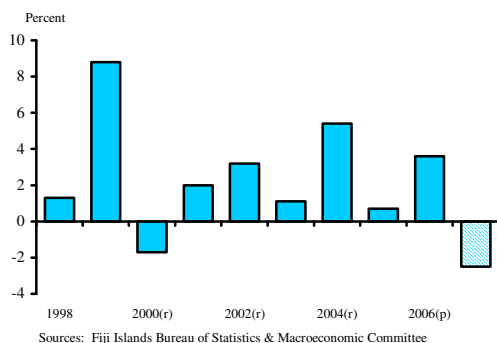
Domestic Economic Conditions

According to the Fiji Islands Bureau of Statistics (FIBOS), the domestic economy is estimated to have registered a growth of 3.6 percent last year (Graph 13). The main sectors which underpinned growth included the finance, insurance, real estate & business services; wholesale & retail trade and hotels & restaurants; manufacturing; building & construction; community, social & related services and electricity & water.

In contrast, declines were recorded in the mining & quarrying; transport & communication and agriculture, forestry, fishing & subsistence sectors.

Graph 13

GDP Growth Rate



This year, however, the economy is projected to decline by 3.1 percent, largely as a result of lower Government spending and a contraction in the building & construction, wholesale & retail trade and hotels & restaurants sectors.

Sectors that are expected to contribute positively to growth are: finance,

insurance, real estate & business services; manufacturing; agriculture, forestry, fishing & subsistence and electricity & water sectors.

Consumer Spending

In the June quarter, partial indicators of **consumer spending** denoted a slowdown. Lending for consumption purposes and currency in circulation slowed in the year to June, when compared to the same period last year. In addition, net Value Added Tax (VAT) collections for the first half of this year totalled \$202.7 million, a decline of around 8.4 percent over the 2006 corresponding period.

In contrast, data on household incomes suggest buoyant growth in the review quarter. Cumulative to June, Pay As You Earn (PAYE) collections, a partial indicator of incomes, rose by around 1.9 percent over the corresponding period last year. Consumer spending has slowed underpinned partly by lower borrowing for consumption purposes as well as lower remittances. Remittances showed an annual drop of 36.2 percent cumulative to April.

Production

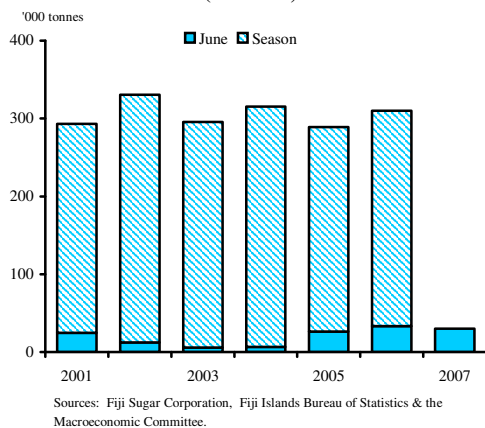
With the exception of the fisheries and timber industries, economic performances of Fiji's major sectors were largely weak during the review period. Visitor arrivals, sugar, garments and copra production fell in the year to June and only marginal

growth was recorded in electricity generation.

Although crushing largely began on schedule, sugar output in the first month of the 2007 crushing season was weak.¹ On a seasonal basis, latest statistics from the Fiji Sugar Corporation (FSC) indicated that a little over 30,000 tonnes of sugar was produced in the first month of the crushing season (Graph 14). This represents a decline of 10.0 percent over the comparable period last season. The lower sugar production was underpinned by low cane supply and operational and plant problems.

Graph 14

Sugar Production (Seasonal)



In the **tourism** industry, provisional data from the FIBOS indicated that cumulative to June, visitor arrivals totaled almost 240,000, a decline of 5.1 percent when compared to the same period last year. The actual level of visitor arrivals in the

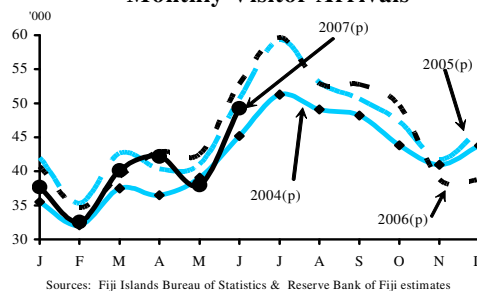
¹ The 2007 crushing season began on schedule, with the commencement of crushing at the Rarawai and Labasa Mills on, 5 June, 2007. However, due to insufficient cane supply, the Penang Mill began crushing on 6 June with the Lautoka Mill commencing a day later.

review period was better than initial projections made by the Fiji Islands Visitors Bureau by around 5.5 percent.

However, the decline in visitor arrivals may not truly reflect activity in the tourism industry. Airlines have reported that in the current mix of travelers, the 'visiting friends and relatives' category is showing a higher proportion of visitors. The decline in actual tourists, therefore, could be higher, suggesting weaker activity in the hotel sector. In addition, the industry is continuing its discount packages which is expected to adversely affect tourism earnings this year (Graph 15).

Graph 15

Monthly Visitor Arrivals



As a result of low demand, the national carrier – Air Pacific Limited – suspended flights from Nausori Airport to Sydney, Auckland and Brisbane towards the end of June until December 2007. Also reduced, from early June, were weekly flights to Nadi from Auckland (from 14 to 11), Sydney (from 11 to 7), Brisbane (from 7 to 6) and Japan (3 to 2).

The lifting of Public Safety Regulations at the beginning of June has not translated to increased ticket sales and bookings for the national airline. However, a positive spin-off from this saw the Australian Government downgrade its travel advisory

on Fiji from Level 3 (high degree of caution) to Level 2 (exercise caution) a week after the Regulations were lifted. New Zealand, on the other hand, has scaled up its travel advisory on Fiji.

On positive developments, the Shangri-La Fijian Resort opened its events centre during the June quarter. The centre is reported to be the largest stand-alone meeting facility in Fiji and would cater for meetings, functions and also provide a boost to the international events market for Fiji. In addition, the South-pacific.travel also launched a series of websites that highlight activities offered by various South Pacific destinations. This was an attempt to better market the unique attractions of South Pacific tourism.

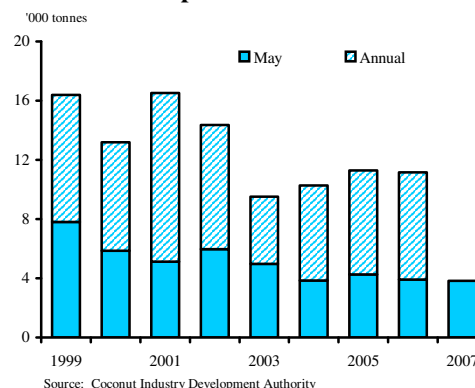
The performance of the **garment** industry remained weak in the review period. Cumulative to April, garment export earnings amounted to \$32.5 million (from \$35.6 million in the comparable period in 2006), representing an 8.6 percent decline.

The Vatukoula **gold** mine remained closed in the review period. In recent developments, the new owner of the mine (Westech International Pty Limited) entered into a partnership with a Canadian financier (Red Lion Management Limited) to finance operations at the mine. However, the commencement of production is dependent on successful negotiations between the gold mining company and the Interim Administration.

Copra industry recorded a weak performance in the year to May, as copra production in the first five months of 2007 amounted to 3,838 tonnes (Graph 16), an annual fall of 2.2 percent.

The minimum mill gate price of copra remained unchanged at \$500 per tonne at the end of May. The producer price (\$534.16) was higher than the mill gate price, as such subsidies were not provided by the Government.

Graph 16

Copra Production

Sources of **electricity** production were diversified as the Butoni Wind Farm came on line, producing electricity from the first week of May, 2007.

However, electricity production was largely subdued in the review period. Cumulative to June, electricity generation registered a marginal growth of 1.2 percent to total 390,304 mega watt hours (Mwh) from 385,530 Mwh recorded in the comparable period in 2006.

In the first four months of 2007, the **fisheries** industry achieved a favourable outcome. Fish export receipts amounted to \$31.2 million, 7.5 percent higher than the 2006 comparable period.

Also buoyant was the performance of the **timber** industry. Export receipts in the first four months of 2007 totalled \$15.7 million, a 56.3 percent increase over the corresponding period last year. For 2007,

the completion of the Wairiki, Bua Port is anticipated to boost pine production in Vanua Levu, which coupled with increased mahogany production, is expected to underpin the 8.0 percent growth envisaged for the timber industry in 2007, after the contraction of 9.3 percent registered last year.

The **building and construction** sector had a noticeably weak performance in the first quarter of 2007. According to the March 2007 Building and Construction Survey Report released by the FIBOS, the total value of work put-in-place in the first quarter of this year totalled around \$59.0 million, representing a significant decline of 26.4 percent over the comparable 2006 period. By category, the value of work put-in-place by the private sector declined substantially by 28.9 percent (from \$63.3 million to \$45.0 million). Value of work in the public sector also fell by 17.1 percent (from \$16.8 million to \$13.9 million).

The first half of the year saw the completion and opening of several projects: the Radisson Resort Fiji on Denarau Island (investment value of \$96.0 million), the Shangri-La Fijian Resort's Ratu Makutu Events Centre (\$12.5 million) in Sigatoka, Likuliku Lagoon Resort (\$32.0 million) and Mid City Plaza (around \$11.5 million). In addition, the Port Denarau and Commercial Centre (\$45.0 million) are expected to officially open in September this year while in Nausori, the \$300 million Haven Project is already underway.

However, a couple of large projects had been put on hold for nearly half the year. Management and land issues halted the Natadola Bay Project. The Momi Bay Resort on the other hand, experienced

delays as a result of issues surrounding the advance tax assessment policy.²

The Apollo Project, a \$100 million development in Lautoka, is a potential investment for the future. The developers and Government agencies are currently negotiating lease approvals.

In line with the forecasted decline in the building & construction sector this year, partial indicators suggest lower **investment** levels. Cumulative to April 2007, imports of investment type goods fell by 9.6 percent when compared with the corresponding period in 2006. Lending to private individuals for housing and investment purposes (includes lending to building & construction and real estate) also slowed. These statistics suggest investment this year will be much lower than the 19.0 percent of GDP level estimated for 2006.

Public Finance

For 2007, Government maintains its target deficit of 2 percent of GDP (Graph 17).

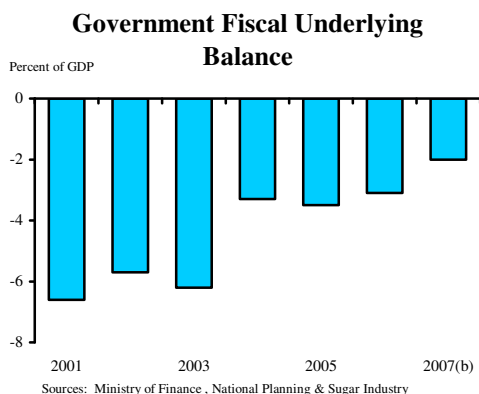
Cumulative to March, cash flow data indicated that Government recorded a net surplus of \$15.0 million, equivalent to 0.3 percent of GDP. This compares with a net surplus of \$48.3 million (1.0 percent of GDP) recorded in the corresponding period last year.

The fiscal outturn in the three months to March was underpinned by a 0.4 percent decline in expenditure payments, which in absolute terms outweighed the 11.1 percent decline in revenue collections

² This refers to the taxing of land sales prior to the actual sale and settlement of funds. The policy was introduced in 2005.

(excluding asset sales).

Graph 17



Government expenditure declined on an annual basis by 0.4 percent, underpinned by a 45.1 percent decline in investing payments. Notably, capital expenditure in the review period rose by 12.9 percent on an annual basis. However, capital expenditure was below target by a significant 84.6 percent. Compared with the forecast for the period, total expenditure was lower by 39.7 percent.

In addition, cumulative to March, Government revenue declined by 11.1 percent when compared with the corresponding period in 2006. The decline in revenue collections stemmed from annually lower direct taxes³ (-3.9 percent) and indirect taxes⁴ (-6.0 percent), particularly VAT collections which declined by an annual 15.9 percent. Revenue collections were lower by 3.4 percent when compared with the budgeted level. While PAYE and VAT collections were higher by 3.7 percent and 8.0 percent

³ While PAYE collections increased on an annual basis by 6.2 percent, company tax collections declined by 11.8 percent.

⁴ Fiscal duties increased by 3.0 percent, import excise rose by 1.6 percent and excise duties increased by 5.6 percent.

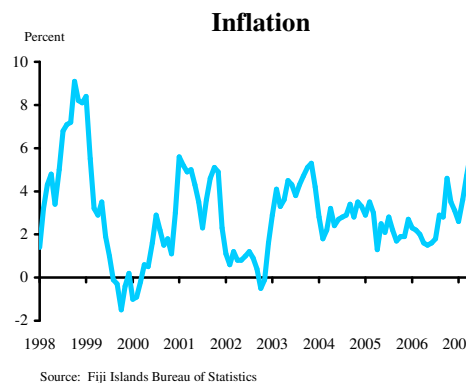
respectively, duties (fiscal, import excise and excise) and company tax collections were lower than budget.

Government's outstanding debt at the end of June 2007 totalled \$2,833.8 million, equivalent to 50.7 percent of GDP. This compares with the outstanding debt level at June 2006 of \$2,524.9 million, or 46.5 percent of GDP.

Inflation

Inflation rose to 7.1 percent in June compared to 4.7 percent recorded in March (Graph 18). On a quarterly basis, consumer prices increased by 2.5 percent. The largest contribution to June inflation came from higher prices of food items namely vegetables & root crops, fresh meat and dairy products. Supply constraints in both domestic (market produce) and external (wheat and dairy) primary industries have consequently led to exorbitant food prices in recent months. Higher prices were also noted for miscellaneous items, alcoholic drinks & tobacco and transport, all of which were largely caused by a rise in imported prices and high duties.

Graph 18



Trimmed mean inflation, a measure of

core inflation, rose to 3.2 percent in June compared to 2.9 percent in March. The gradual increase in core inflation since last year is partly a reflection of second round effects of the oil price hikes in recent years and the lagged effect of persistent and strong growth of money and credit in past years.

In the approaching months, inflationary pressures are expected to mount, given that continuing domestic and external supply constraints are expected to keep food prices high. Externally, the episodic droughts in Australia are most likely to keep the prices of bakery, wheat, cereal and dairy products high. Some of these effects have already filtered into higher domestic prices but more increases are likely in the coming months. Domestically, market produce prices will probably remain buoyant because higher exports of fruits and vegetables to foreign markets are constraining domestic supply.

Furthermore, the increase in global oil prices experienced during the quarter will pass through into domestic retail prices of fuel in the September quarter. It is also likely that the higher global oil prices could raise the electricity fuel surcharge as well.

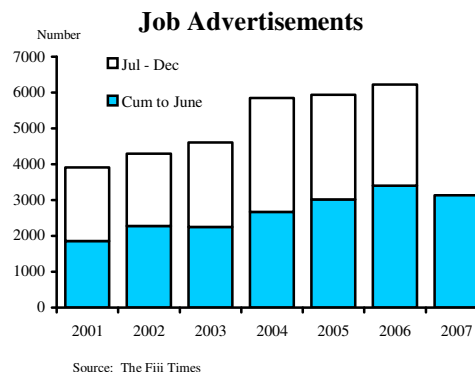
In light of the above factors, the current year-end inflation forecast of 3.5 percent has been revised to around 7.0 percent.

Labour Market

In line with the current economic climate, conditions in the labour market remain soft. The job advertisements survey, cumulative to June, noted a fall in employer recruitment intentions by around 7.8 percent (3,398 to 3,133) over the corresponding period last year (Graph 19).

Weaker employment prospects were largely noted in the finance, insurance, real estate & business services; electricity & water; mining & quarrying and construction sectors.

Graph 19



However, anecdotal evidence and partial indicators seem to suggest the contraction in employment levels noted at the end of 2006 and in the early months of 2007 were generally contained in the mining industry and the tourism sector. In the months of January to June this year, around 7,300 employees were registered as new taxpayers with the Fiji Islands Revenue & Customs Authority, an annualised increase of around 30.1 percent. This was primarily led by the community, social & personal services sector followed by the wholesale, retail trade, restaurants & hotels; finance, insurance, real estate & business services and manufacturing sectors.

It should be noted, however, that the increase in newly registered taxpayers does not necessarily reflect the creation of new jobs. They also represent existing vacant positions that have been filled, delayed registering of existing workers as taxpayers or even workers who have entered the taxable bracket as a result of

salary increases.

The External Sector

Recent export data showed some encouraging signs. Following consistent declines on an annual basis up to April, latest accrual trade data showed merchandise exports rose by around 3.5 percent cumulative to May 2007. This compares with a decline of 8.5 percent in the corresponding period last year. Domestic exports rose by 12.3 percent.

Leading the increase in receipts were sugar, other domestic exports, fish, timber, fruits & vegetables, coconut oil and yaqona. These more than offset the declines recorded in sectors such as re-exports, gold, molasses, textiles, yarn and fabric.

During the same period, merchandise imports declined by around 7.9 percent, compared to a growth of around 18.0 percent in the corresponding period in 2006. All categories of imports declined with the main driver being investment goods (-14.6 percent). Consumption and intermediate goods fell by 6.3 percent and 3.2 percent respectively.

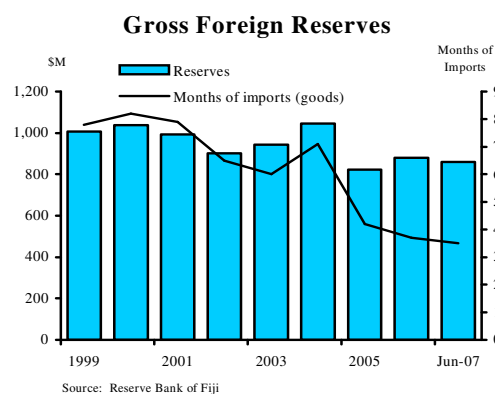
The slowdown in outflows for investment goods (-14.6 percent) was attributed to lower payments for machinery, transport equipment and chemicals. The decline in import payments for consumption goods (-6.3 percent) was led by manufactured goods, miscellaneous manufactured goods, and beverage and tobacco. The decline in intermediate goods (-3.2 percent) was attributed to mineral fuels and crude materials.

Excluding re-exports of mineral fuels, exports increased by around 10.2 percent

cumulative to May 2007, compared to a decline of 12.3 percent in the same 2006 period. Excluding mineral fuels, imports declined by 9.8 percent cumulative to May this year, compared to a growth of 14.4 percent in the same period in 2006.

Foreign reserves at the end of June were around \$859.9 million, sufficient to cover 3.5 months of import payments of goods (Graph 20).

Graph 20



Domestic Financial Conditions

Money Markets

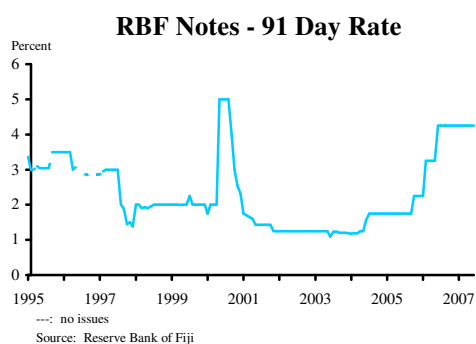
Interbank activity fell in the June quarter, with total turnover amounting to \$6.1 million, a 60.6 percent decline from the March quarter. This was largely a reflection of better liquidity conditions. As a result, the weighted average interbank rate fell to 4.22 percent, down from 5.25 percent in the previous quarter.

During the review quarter, the monetary policy stance remained unchanged with the indicator rate maintained at 4.25 percent (Graph 21). However, while maintaining the credit ceiling, the Reserve Bank reduced the Statutory Reserve

Deposit ratio (SRD) from 7 percent to 6 percent from 1st May and relaxed exchange control approval processes for advance import payments on 8 June. Only advance import payments over F\$15,000 will require Reserve Bank approval.

On open market operations, \$92.0 million worth of RBF Notes was allotted in the June quarter, at a weighted average yield of 4.25 percent. There was no issue of RBF Notes in the March quarter.

Graph 21



Government issued \$191.7 million worth of Treasury Bills during the review quarter, \$20.6 million higher than the March quarter. The interest rate on Government's 91-day T-Bills averaged 4.56 percent during the June quarter, down from 11.0 percent in the previous quarter.

Capital Markets

Government issued bonds worth \$19.3 million during the second quarter of 2007, much lower than \$39.2 million issued in the March quarter. Maturities were spread between 3, 5, 7, 10 and 15 years.

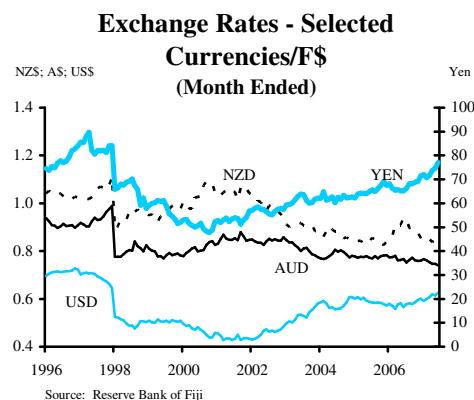
The Fiji Development Bank issued bonds with overall shorter maturities ranging from 1 to 3 years, to total \$24.2 million in

the June quarter, compared with \$11.2 million in the first three months.

Foreign Exchange Markets

Quarterly comparisons of bilateral exchange rates showed the Fiji dollar strengthened against the Japanese Yen (7.7%), US dollar (3.1%) and Euro (2.2%) but weakened against the New Zealand (4.3%) and Australian dollars (1.8%) in June 2007 (Graph 22).

Graph 22

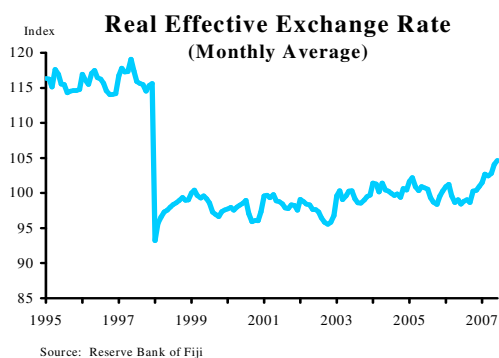


The Nominal Effective Exchange Rate Index (NEER), which reflects aggregate exchange rate movements between the Fiji dollar and currencies of major trading partners, rose over the June quarter by 0.3 percent, indicating an appreciation of the Fiji dollar against the basket of currencies.

During the same period, the Real Effective Exchange Rate Index (REER) of the Fiji dollar, which adjusts the NEER for inflation differentials across Fiji's major trading partners rose by 2.2 percent (Graph 23). The rise in the REER reflects a deterioration in Fiji's international competitiveness. The increase was underpinned by higher domestic inflation which was 7.1 percent in June compared to 4.7 percent at the end

of the March quarter.

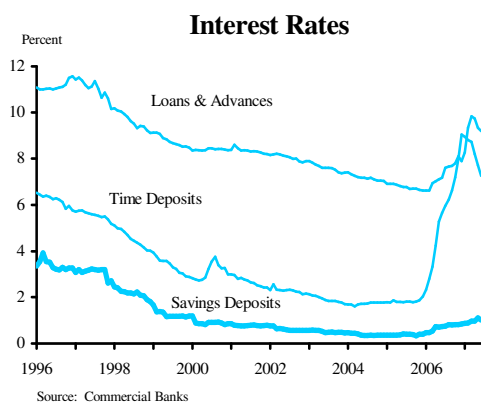
Graph 23



Financial Intermediaries

Reflecting improved liquidity conditions during the review period, commercial banks' interest rates continued to trend downwards. In comparison to the March quarter, the time deposit rate fell by 146 basis points to 7.27 percent (Graph 24).

Graph 24



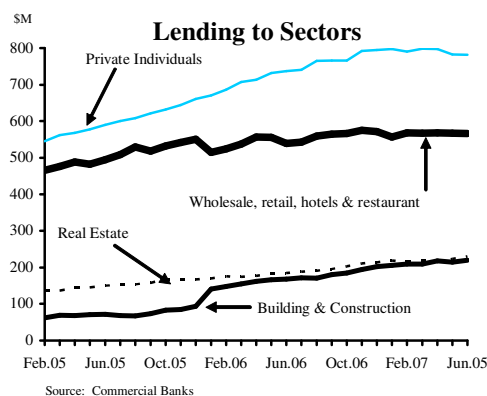
In addition, interest rates on new time deposits fell by 315 basis points to 5.23 percent in June. On the upside, the savings deposit rate rose by 3 basis points during the same period, to 1.01 percent.

The weighted average lending rate on outstanding loans declined to 9.20 percent

over the June quarter, while the interest rate on commercial bank new loans fell by 152 basis points to 10.02 percent.

With the credit ceiling currently in place, commercial banks' outstanding credit slowed further during the quarter and grew by only 11.4 percent in the year to June, down from 16.2 percent in March. Lending to private individuals (mainly for housing and other purposes), and the building & construction, manufacturing, real estate and wholesale & retail trade sectors continued to drive credit demand (Graph 25).

Graph 25



Lending by Licensed Credit Institutions (LCIs)⁵ also slowed in June, growing by 5.8 percent, down from 8.6 percent in the year to March.

Interest rates offered by LCIs portrayed mixed movements. The weighted average lending rate rose by 39 basis points to 12.78 percent in June, while the interest rate on time deposits decreased to 7.41 percent in June, from 9.13 percent in March.

⁵ LCIs' include Merchant Finance Investment Company Limited, Credit Corporation (Fiji) Limited and Home Finance Company Limited.

Banking Industry Quarterly Condition Report – March 2007

Overview - Commercial Banks

The **overall condition** of the banking industry was assessed as satisfactory, despite a slight contraction in the banks' combined balance sheet and a drop in profitability in the March quarter. Capital remained strong against marginal ratings for earnings and liquidity.

Total assets recorded a slight contraction of 0.5 percent to \$3.4 billion following decreases in balances due from bank counterparties (foreign currency deposits and exchange settlement balances), as banks managed this decrease to meet liquidity needs.

The overall banking industry recorded a strong **capital adequacy ratio** of 12.1 percent.

Asset quality remained satisfactory, although impaired and classified loans increased for the second consecutive quarter. As a result, general provisions were raised by all banks over the quarter. Closer monitoring is warranted considering the rise in past due and special mention accounts.

Management is rated as satisfactory, reflecting strong capital positions and capable management of liquidity and asset quality over the quarter.

Earnings were assessed as marginal in the March quarter. Pre-tax quarterly profits dropped and the efficiency ratio deteriorated.

Liquidity remained marginal as banks' stock of liquid assets fell further over the

quarter. This was also reflected in the deterioration of liquidity ratios recorded by most banks.

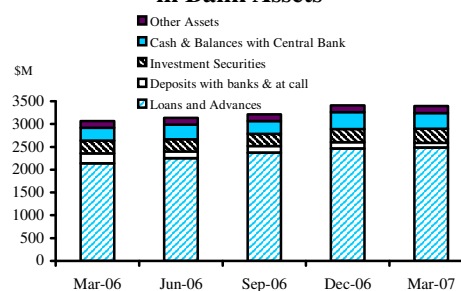
Balance Sheet

After recording consecutive quarterly growth since March 2004, the banking industry's balance sheet contracted by 0.5 percent in the March 2007 quarter to \$3.4 billion (Graph 26).

However, on an annual basis this grew by \$328.3 million or 10.7 percent from \$3.1 billion in March 2006. The annual growth rate slowed from 16.6 percent recorded in December 2006.

Graph 26

Structural Change and Growth in Bank Assets

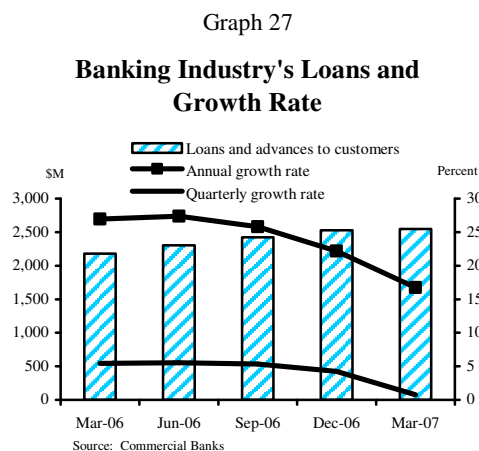


Source: Commercial Banks

In terms of structural changes in banks' assets, balances owing from other banks recorded a reduction of \$31.7 million over the quarter and \$116.5 million over the year, to \$105.8 million. Cash and balances with the central bank also fell by \$28.7 million over the quarter and \$10.1 million over the year. Funds were mainly utilised to meet outflows.

Total loans and advances of the banking industry edged up over the quarter but at a slower rate (0.8%) compared with the previous quarters (Graph 27). The

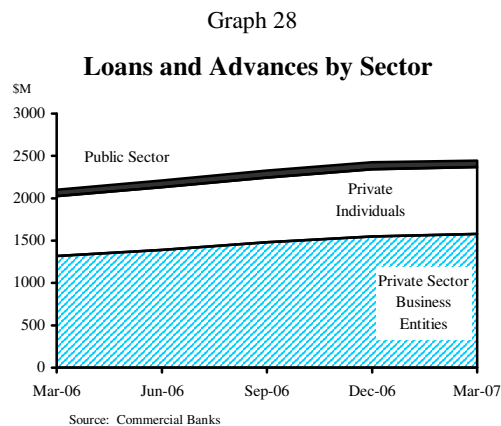
significantly slower quarterly growth was a direct result of the credit ceiling implemented in early December 2006. The annual growth rate also slowed as reflected in the graph.



Credit to the public sector fell by 6.4 percent in the March quarter as loans to the central government declined. However, over the year, loans to central and local government increased by 3.0 percent.

An analysis of the sectoral breakdown shows that private sector business credit was largely directed towards high priority sectors over the quarter. The manufacturing and building & construction sectors recorded the highest increases of \$10.2 million and \$7.3 million respectively, while the transport & storage and electricity, gas & water sectors recorded smaller growth. Among the low priority areas, lending to private individuals and wholesale & retail sectors declined by \$5.4 million and \$5.0 million respectively, while credit to the real estate and professional & business services sectors continued to increase over the quarter by \$9.4 million and \$3.1 million,

respectively (Graph 28).



With the exception of one bank, all banks showed a quarterly decline in lending to private individuals. With a restricted lending approach taken by banks, credit to private individuals declined by 0.7 percent over the quarter while the annual growth rate slowed from 26.0 percent a year ago to 12.8 percent in March.

On the liabilities side, increases were noted in balances due to banks. Bills payable also showed quarterly and annual increases. Borrowing from Reserve Bank was recorded in the March quarter.

The reduction in major liquid assets of the industry (deposits with banks and cash and settlement balances) and increased levels of short-term liabilities, reflected the tight liquidity situation faced by banks at the time.

After continuous growth in deposit levels since March 2004, the banking industry recorded a net decline in deposits of \$80.4 million in the current quarter. This was mainly caused by private sector business entities utilising their demand deposits. Savings deposits also decreased by \$7.2 million. Time deposits, however,

increased by \$32.4 million mainly due to deposits placed by private sector businesses and non-bank financial institutions taking advantage of higher term interest rates. Some movement of time deposits across banks was also noted as depositors moved funds based on interest rates offered by the different institutions.

On an annual basis, deposits continued to show an overall increase of \$220.0 million, as the majority of funds accumulated in previous quarters remained in the system. The March quarter showed a large movement of deposits from demand (-\$120.3 million) and savings (-\$31.2 million) to time (+\$501.2 million) as customers took advantage of the high interest rates offered by banks.

Capital Adequacy

Overall, a strong capital adequacy ratio of 12.1 percent was recorded for the banking industry in the March quarter. On an individual basis as well, banks recorded strong capital adequacy ratios. March quarter's ratio compares to 11.7 percent recorded in the previous quarter and 11.3 percent a year ago (Graph 29).

The improvement over the quarter was mainly due to a faster rate of growth in capital (5.1 percent) over growth in risk-weighted assets (0.9 percent). Total capital grew, as unaudited profits accumulated in the tier 2 capital category. Risk weighted assets recorded decreases in all categories except those with 100 percent risk weighting.

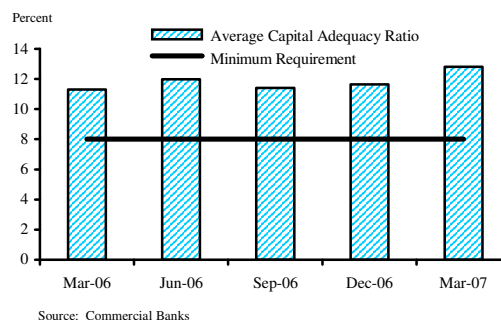
This was a direct impact of the credit ceiling and a generally tighter liquidity situation for banks, which saw less-than-

usual loan approvals and a decline in liquid assets.

Capital levels are expected to drop in the next quarter with two major banks expected to remit profits to their head offices.

Graph 29

Capital Adequacy Ratio of Banks



Asset Quality

The impact of hikes in commercial interest rates is now reflected in the asset quality of banks. Despite a deterioration in the overall asset quality position over the March quarter, prudential indicators still rate asset quality as satisfactory. With the exception of one major bank, the asset quality of banks suffered as the level of past due loans increased over the quarter.

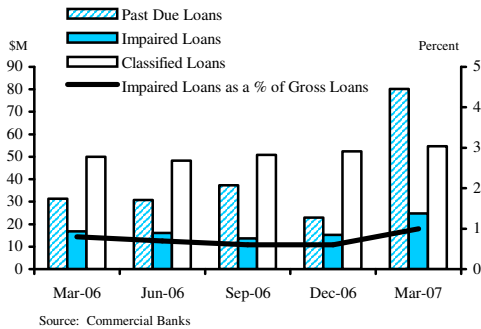
The level of classified loans increased by 4.2 percent over the quarter and 9.4 percent over the year, to \$54.7 million, mainly reflecting an increase in the loss category. In addition, special mention accounts increased significantly in the March quarter by \$23.9 million (63.1 percent) to \$61.8 million.

Out of the \$54.7 million classified loans, \$24.7 million were impaired in the March quarter. These levels increased by \$9.6

million over the quarter and \$8.0 million over the year. Impaired assets comprised 1.0 percent of gross loans compared to 0.6 percent in the previous quarter and 0.8 percent in March 2006 (Graph 30).

Graph 30

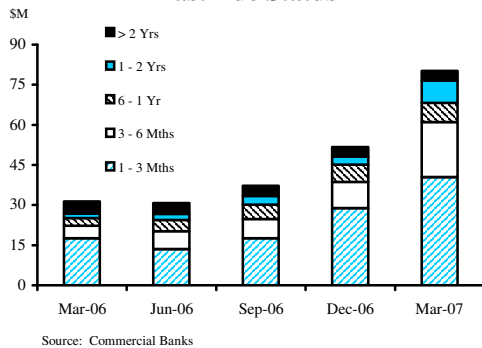
Asset Quality



Higher interest rates have fuelled the increase in past due loans over the last two quarters with the March quarter (55.1 percent) recording a significant increase over the 38.8 percent recorded in the previous quarter. The increase in past due loans was mainly in the 1-3 months and 3-6 months categories (Graph 31).

Graph 31

Past Due Status



The banking industry’s problem loans are concentrated in the private individuals sector (42.2 percent) led by housing loans which makes up 35.5 percent of total

problem loans. Private individuals’ problem loans increased by 5.5 percent (\$2.5 million) over the quarter and 62.0 percent (\$18.2 million) over the year.

Over the quarter, the wholesale & retail sector recorded the highest increment in terms of value (\$10.2 million) followed by the real estate sector (\$6.6 million). Annual comparisons indicate that in March 2006, there were no problem loans in the real estate sector. Problem loans in the wholesale & retail sector however, are now \$15.3 million higher than a year ago. Over the year, a reduction of \$4.7 million was noted for problem loans in the mining sector.

Corresponding to the increase in impaired accounts, total provisions increased to \$49.1 million, an increase of \$2.3 million over the quarter and \$16.7 million over the year. The quarterly increase was mainly recorded in specific provisions (\$1.5 million). However, over the year, a much higher increase was recorded in general provisions (\$16.8 million). Banks commenced a build-up in general provisions from March 2006, in anticipation of a possible deterioration in asset quality following the monetary policy tightening and expected higher interest rates.

As at March 2007, general provisions represented 1.6 percent of gross loans and advances, an increase from 1.1 percent in March 2006.

Banks did not raise specific provisions to match the increase in the level of impaired accounts as reliance was placed on collateral held on these accounts. Based on a case-by-case analysis, provisions held on individual accounts may be assessed as adequate.

The current level of classified and past due loans is considered moderate. However with the rising past due levels and special mention accounts, asset quality requires close monitoring.

Earnings

In the March quarter, the banking industry registered a \$24.0 million pre-tax profit. This compares to \$28.1 million in the previous quarter and \$32.6 million in March 2006. The decline in quarterly profits was caused by lower non-interest income and an increase in operating expenses.

Arising from the tightening of monetary policy, large increments were recorded in interest expenses over the year. Interest rates on lending were also raised to cushion the impact of high rates of interest paid on deposits, which is reflected by the increased interest income.

Non-interest income fell over the quarter mainly due to a reduction in income earned from foreign exchange business.

Operating expenses increased both over the quarter and the year. This mainly stemmed from management expenses as one bank paid its head office for an upgraded technology platform.

With an anticipated deterioration in asset quality, banks expensed \$3.6 million as bad and doubtful debts over the quarter. This was a large increment compared to \$0.7 million expensed in the previous quarter and a write-back of \$0.2 million in March 2006.

Banks' Combined Income Statement

	Mar 06	Dec 06	Mar 07	% Change	
				Over Qtr	Over Mar 06
Interest Income	42.2	63.5	70.5	11.1	67.2
Interest Expense	6.5	28.8	34.3	19.4	429.0
Net interest income	35.7	34.7	36.2	4.3	1.4
Add: Non interest income	23.0	22.8	22.2	-2.5	-800
Income from overseas exchange transactions	8.8	9.2	8.8	-4.1	0.4
Commission	4.3	3.5	3.5	-0.2	-17.7
Fee Charges	9.8	8.8	9.8	11.1	0.3
Other income	0.2	1.3	0.1	-90.4	-44.5
Total operating income	58.7	57.5	58.4	1.6	-0.5
<i>Less: Operating expenses</i>	<i>26.3</i>	<i>28.7</i>	<i>30.7</i>	<i>7.2</i>	<i>17.0</i>
<i>Less: Bad Debts & provisions</i>	<i>-0.2</i>	<i>0.7</i>	<i>3.6</i>	<i>427.7</i>	<i>2030.0</i>
Profit before tax	32.6	28.1	24.0	-14.5	-26.3
<i>Less: Tax</i>	<i>10.2</i>	<i>8.3</i>	<i>8.1</i>	<i>-2.6</i>	<i>-20.7</i>
<i>Add Extra ordinary items</i>					
Net profit after tax	22.4	19.8	15.9	-19.5	-28.8

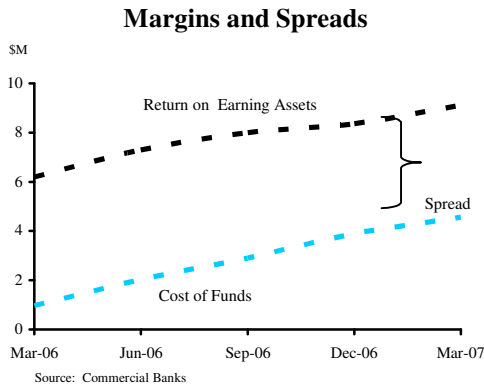
Source: Commercial Banks

The reduction in before-tax profits consequently impacted the return on assets (annualised), which reduced to 2.8 percent from 3.4 percent in the previous quarter and 4.4 percent in March 2006. Similarly, the return on equity reduced to 24.4 percent from 31.9 percent in December and 40.4 percent in March 2006.

Interest Margin and Spread

Over the quarter, the return on earning assets and the cost of funds for the banking industry both increased further (Graph 32).

Graph 32



The yield on earning assets increased by 74 basis points to 9.1 percent while the cost of funds rose by 65 basis points to 4.6 percent, resulting in a widening of the spread by 9 basis points.

Heavy competition for funds led to sharp increases in wholesale deposit rates throughout last year. Banks responded by increasing their lending rates to partly transfer the higher costs to their customers. As a result, together with the cost of funds, the yield on earning assets also recorded consistent growth over the quarters.

The cost of funds is expected to reduce over the next few quarters with more recent falls in carded deposit rates. Lending rates are also expected to fall in the following quarters.

Efficiency

In March 2007, the efficiency ratio of banks (operating costs to operating income) deteriorated to 52.6 percent. This compares to a ratio of 49.9 percent in December 2006 and 44.8 percent in March 2006. The quarterly decline was a result of a higher rate of increase in operating expenses (7.2 percent) than in

operating income (1.6 percent). Over the year, the deterioration was the combined result of an increase in operating expenses (17.0 percent) and a reduction in operating income (0.5 percent).

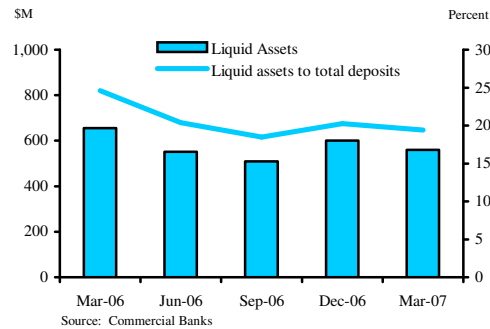
Liquidity and Funding

Overall banks’ liquidity position is assessed as marginal. Liquid assets, at \$559.3 million, decreased by \$40.8 million over the quarter and \$96.1 million over the year. This was attributed to a major decline in deposits with banks and cash and settlement accounts.

Arising from the drop in liquid assets, the industry’s coverage of total deposits deteriorated both over the quarter and over the year. This was also reflected in the coverage of total liabilities and the overall loans to deposits ratio which stood at 88.3 percent at the end of the quarter. This compares to 85.2 percent in December 2006 (Graph 33).

Graph 33

Liquid Assets to Total Deposits



As at March 2007, \$714.4 million of deposits were held by the 15 largest depositors of the industry.

The maturity profile of the banking industry shows a negative mismatch of

\$494.4 million within the next 6 months. This compares to the positive mismatch of \$176.9 million in the less than 1 month category and the negative flows of \$548.5 million up to 6 months in the previous quarter. Liquidity was tighter this quarter with the increase in short-term outflows.

Liquidity is expected to improve in the next few quarters with the lowering of the SRD holding requirement from 1st May. However, close monitoring of liquidity will continue.

Overview – Credit Institutions

The **overall performance** of credit institutions was assessed as satisfactory during the quarter.

The **consolidated balance sheet** recorded a slight contraction of 0.4 percent in the March quarter to \$345.5 million.

Capital adequacy remained strong at 23.5 percent, well above the 10 percent minimum requirement.

With increases in past due levels, **asset quality** ratios continued to be rated as marginal. All institutions envisaged the deterioration in asset quality and consequently raised their general provisions.

Management of credit institutions is assessed as satisfactory. Despite poor liquidity levels, cash flows were managed adequately to meet obligations. A proactive approach was taken towards asset quality and capital was maintained at strong levels.

Earnings were marginal with declines in

all profitability ratios and a deterioration in efficiency. March quarterly profits declined to \$2.9 million from \$4.0 million in the previous quarter and \$4.2 million in March 2006.

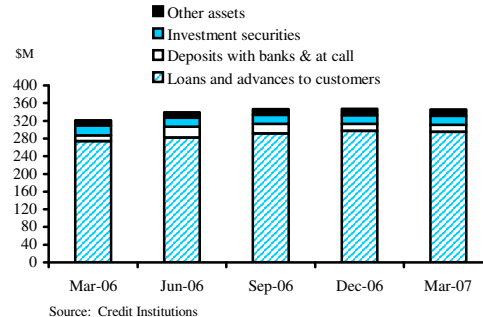
Liquidity of credit institutions is assessed as marginal due to the low levels of liquid assets held and heavy dependence on shareholder borrowings to meet maturing obligations.

Balance Sheet

Credit institutions' balance sheet fell by 0.4 percent to \$345.5 million (Graph 34). The contraction over the quarter was a result of a decline in total loans and term deposits and other liabilities. The annual growth of 7.6 percent was the slowest since December 2002 (5.6 percent).

Graph 34

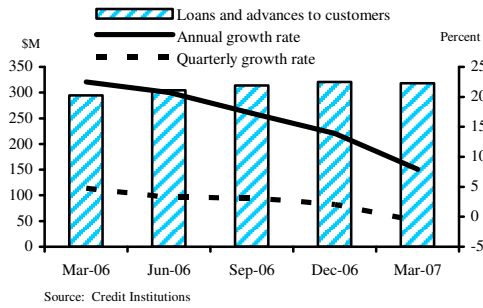
Structural Change and Growth in Credit Institutions' Assets



Total loans declined by 0.7 percent over the quarter to \$318.1 million. Growth was mixed across the three credit institution's portfolios. On an annual basis, loan growth has slowed significantly, by 7.5 percent from 13.1 percent in the previous quarter (Graph 35).

Graph 35

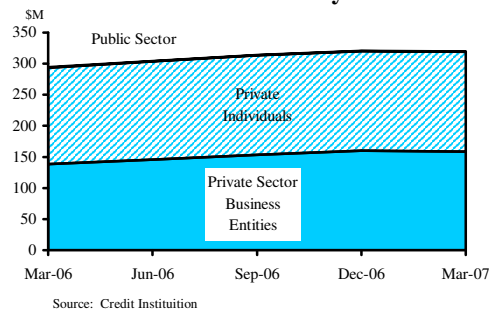
Credit Institutions' Loans and Growth Rate



On a sectoral comparison, over the March quarter, private sector business loans declined by 1.0 percent while private individual loans increased by 0.4 percent. Public sector loans remained constant. On an annual basis, however, both private business and private individual loans increased, while public sector loans declined (Graph 36).

Graph 36

Loans and Advances by Sector



Similar to banks, credit institutions also recorded a decline in their deposit levels (\$6.0 million) over the quarter to \$188.3 million following continuous growth in all quarters of 2006. However, year-on-year, deposits grew by \$49.7 million.

A direct link between the level of deposits and amounts owing to holding companies was noted. While deposit levels were

higher (\$49.7 million) over the year, amounts owing to holding companies showed a reduction (\$30.0 million). On a quarterly basis, as the level of deposits dropped, amounts owing to holding companies increased, by \$6.6million.

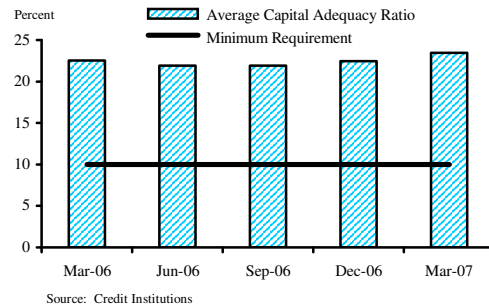
Capital Adequacy

As at March 2007, combined credit institutions recorded a strong capital adequacy ratio of 23.5 percent. This was 132 basis points higher than the previous quarter and 92 basis points higher than March 2006 (Graph 37).

The improvement in capital adequacy was due to a decline in risk-weighted assets, coupled with a growth in total capital to \$58.1 million in March 2007.

Graph 37

Capital Adequacy Ratio of Credit Institutions



Total risk-weighted assets stood at \$247.6 million. The decline in risk weighted assets over the quarter mainly stemmed from the 100 percent risk-weight category as the level of private sector loans declined in the March quarter. On an annual basis, with exception of 10 percent risk-weight category, all other categories registered a growth.

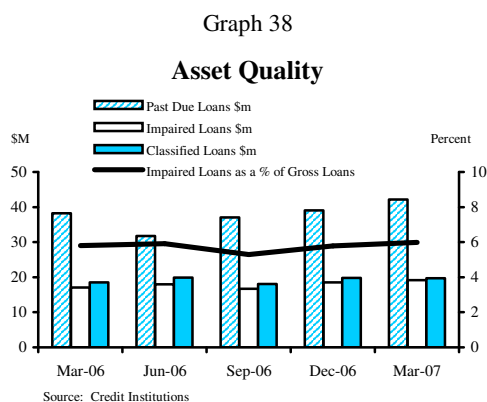
Capital adequacy levels would highly

depend on the individual institution's earnings capability and changes in asset quality over the next few quarters.

Asset Quality

Credit institutions' asset quality remained marginal. Similar to banks, there was a deterioration in asset quality with rising past due accounts (Graph 38).

Classified exposures recorded minimal growth over the quarter but much higher growth over the year. A large increment was also noted in the level of special mention accounts over both the quarter and the year, indicating a probable worsening of asset quality positions in upcoming quarters.



Some loan writeoffs led to a slight decline in all institutions' specific provisions over the quarter. However, all institutions envisaged a deterioration in their asset quality and raised their general provisions by \$0.3 million over the quarter and \$1.4 million over the year, to \$10.7 million.

Earnings

In the March 2007 quarter, the combined credit institutions recorded profits before tax of \$2.9 million, which was assessed as

marginal. This compares to \$4.0 million in the December quarter and \$4.2 million in the March 2006 quarter. Reduced earnings in the March quarter were mainly a result of a reduction in net interest income.

Credit Institutions' Income Statement

	Mar 06	Dec 06	Mar 07	% Change	
	\$M			Over Qtr	Over Mar 06
Interest Income	9.02	11.2	10.8	-3.5	19.6
Interest Expense	2.6	4.4	5.3	21.6	107.3
Net interest income	6.5	6.8	5.5	-19.7	-15.2
Add: Non interest income	1.1	0.6	0.7	11.4	-33.5
Commission	1.0	1.0	0.8	-23.9	-19.3
Fee Charges	0.4	0.5	0.3	-39.2	-27.7
Other income	0.5	0.01	0.3	2779.8	-41.0
Total operating income	7.5	7.5	6.2	-17.0	-17.8
<i>Less: Operating expenses</i>	<i>2.7</i>	<i>2.7</i>	<i>2.8</i>	<i>3.7</i>	<i>6.5</i>
<i>Less: Bad Debts & provisions</i>	<i>0.6</i>	<i>0.8</i>	<i>0.5</i>	<i>-34.6</i>	<i>-18.3</i>
<i>Equals:</i>					
Profit before tax	4.2	4.0	2.9	-28.0	-33.0
<i>Less: Tax</i>	<i>0.7</i>	<i>0.7</i>	<i>0.4</i>	<i>-39.4</i>	<i>-42.0</i>
<i>Add Extra ordinary items</i>					
<i>Equals:</i>					
Net profit after tax	3.6	3.3	2.4	-25.7	-31.3

Source: Credit Institutions

As detailed in the table, net interest income suffered over the quarter due to a 3.5 percent decline in interest income while interest expenses rose by 21.6 percent. Over the year, the change reflected a rise in interest expenses while interest income recorded marginal growth.

Non-interest income recorded minimal changes both over the quarter and over the year. Operating expenses showed slight increases both over the quarter and over the year.

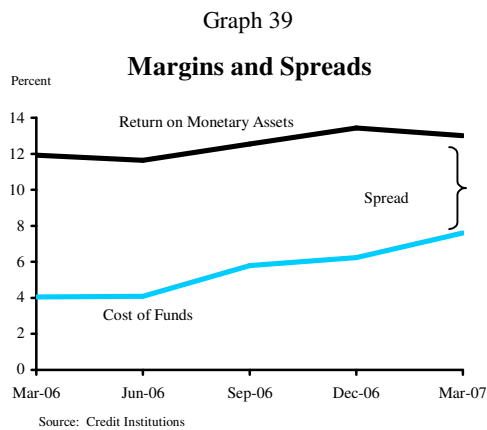
With a reduced loan portfolio, lower amounts were expensed as bad debts and provision expenses this quarter.

Reduced earnings had an adverse effect on profitability ratios. Return on assets (ROA) before tax recorded declines over the quarter (128 basis points) and over the year (212 basis points) to 3.3 percent. Return on equity (ROE) ratio also dropped to 16.9 percent from 23.3 percent in December 2006 and 26.9 percent in March 2006.

The operating expenses to operating income ratio deteriorated further to 45.9 percent from 36.7 percent in the previous quarter and 35.4 percent in March 2006.

Interest Margin and Spread

Credit institutions’ overall spread contracted further in the March 2007 quarter with decreasing yield on earning assets and increased cost of funds (Graph 39).



The yield on earning assets dropped by 44 basis points in the March quarter to 13.0 percent. However, on annual basis it was better than the 11.9 percent recorded in March 2006.

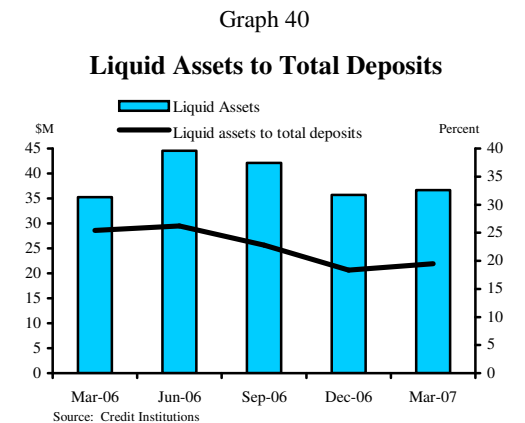
With heavy market competition offered by banks and rising interest rates, the cost of funds continued its upward trend and almost doubled in the current quarter (7.6%) from March 2006 (4.0%).

As banks reduce their deposit rates, rates offered by credit institutions is also expected to reduce in the coming quarters.

Liquidity

The liquidity position of credit institutions in the March 2007 quarter is rated as marginal.

Liquidity ratios improved slightly over the quarter with an increase in the level of liquid assets (Graph 40). This improvement was reflected in increased borrowing from holding companies.



Total liquid assets increased by \$0.9 million over the quarter and \$1.4 million over the year to \$36.7 million. This led to an increased coverage of total deposits over the quarter (from 18.4 percent in December 2006 to 19.5 percent in March). Deposit coverage was better in March 2006 (25.4 percent) as deposits were at lower levels in March 2006. However, while coverage improved, debts to holding

company increased.

Credit institutions' maturity profile shows negative mismatches of \$88.9 million within the next 12 months. With the current level of liquid assets, only 41.2 percent would be met without engaging in additional borrowings. Borrowings from shareholders increased over the quarter by \$6.6 million to \$90.9 million.

The 15 largest depositors make up \$90.2 million or approximately 50 percent of total deposits of credit institutions. Furthermore, the largest depositor, being the major shareholder of one of these institutions, holds 26.5 percent of total deposits with credit institutions.

A simultaneous withdrawal of deposits by these 15 large depositors would mean that credit institutions would not be able to meet these by fully utilising their liquid assets. They would be highly dependent on borrowings to meet these maturing obligations.

Outlook

With the credit ceiling in place and falling deposit rates, both banks' and credit institutions' balance sheets are expected to contract further. Non-priority lending to private individuals is expected to decline.

The liquidity situation for both banks and credit institutions is expected to ease a bit. However, on an overall basis, liquidity is expected to remain quite tight with funds still being directed to loan commitments.

Insurance Industry Quarterly Condition Report – December 2006

Overview

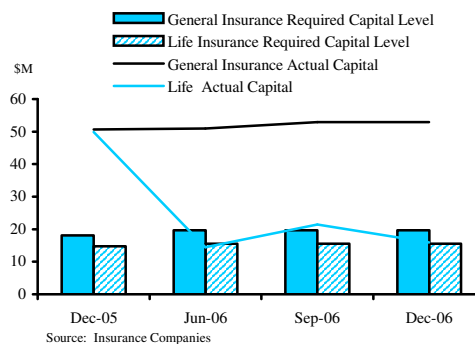
The insurance industry's performance over the quarter is assessed to be satisfactory indicated by the combined industry solvency surplus, adequate level of liquid funds, and a significant improvement in the earnings level of the life industry.

While the life industry recorded a surplus (profit), the significant increase in underwriting expenses by the general insurance industry resulted in it recording a loss during the quarter.

Most of the licensed insurers continued to meet the solvency requirements under the Insurance Act 1998. Further supervisory consultations continue with insurers who reported shortfalls and satisfactory work is currently underway to address these issues (Graph 41).

Graph 41

Insurance Industry Actual Capital & Required Capital Levels

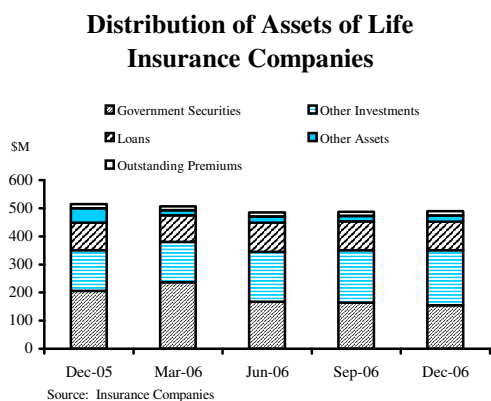


Licensed Insurers

The insurance industry's capital requirement remained unchanged over the quarter at \$48.4 million and the industry's actual holdings was recorded at \$68.5 million, confirming a **capital surplus** holding of \$20.1 million. This surplus is a 61 percent decrease from the same period in 2005 (\$52.0 million).

Combined **assets** of the industry remained at similar levels to the September quarter, recording a slight increase of 1.0 percent (Graph 42). While life insurers continue to hold a larger market share, accounting for 69 percent of the total industry assets, asset growth of the industry continues to be driven by the general sector.

Graph 42



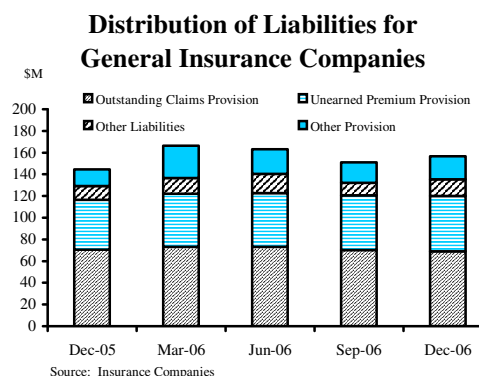
All general insurers continued to have in place adequate **reinsurance arrangements** while life insurers continued to build their reinsurance pool to prepare for unforeseen losses.

Combined **liabilities** (excluding shareholders funds) recorded a marginal increase of 3 percent over the year to \$624.7 million. The life insurers' balance of revenue account continues to form the bulk of insurance industry liabilities at

\$450.0 million (72.0 percent of total liabilities).

Total liabilities of the general insurance industry were recorded at \$157.6 million, a slight increase of 3.0 percent over the quarter and 8.0 percent over the year from \$145.7 million (Graph 43).

Graph 43



The industry reported an overall net profit of \$11.6 million during the quarter, an increase of 8 percent from December 2005, but a decrease of 3 percent compared to the \$11.9 million net profit recorded in September 2006. The decrease over the quarter is a result of the general sector incurring a loss due to the significant increase in its underwriting expenses.

The industry's liquidity position is assessed to be satisfactory with life insurers continuing to hold long-term assets to match their long-term liabilities, while general insurers maintained a \$56.0 million surplus of liquid funds to meet short-term liabilities.

Insurance Brokers

Total revenue of the insurance broking industry grew by 11.0 percent to \$4.1 million whilst total expenses increased to

\$1.9 million.

Total revenue of the insurance broking industry grew from \$3.6 million in the same period of 2005. As in previous quarters, the increase in total revenue is mainly attributed to brokerage earned as commission. This category increased by 7 percent to \$3.7 million in the December 2006 quarter. The components of total revenue remained consistent over the year and the quarter, with brokerage earned as commission accounting for 91 percent of the total revenue.

Total expenses for the December 2006 quarter stood at \$1.9 million, an increase of 21.0 percent over the corresponding period of 2005. A significant increase was noted in other expenses which increased by 21 percent to \$1.0 million.

Insurance brokers' consolidated net profit before tax stood at \$2.1 million, an increase of 4.0 percent over the year and 8.0 percent over the previous quarter. However the after tax profit decreased to \$0.5 million (2005: \$0.9m) largely the

result of an increase in taxation expenses.

The balance in the Insurance Broking Account decreased by 29 percent over the year to \$2.9 million at the end of the December 2006 quarter.

A total of 97 **offshore applications** amounting to \$10.8 million were approved compared to 111 offshore approvals amounting to \$5.2 million in the previous quarter, and 104 approvals totalling \$11.3 million in the same period of 2005.

Outlook

With the expected contraction of the economy during 2007, the growth of the insurance industry is projected to slow. During times of economic slowdown, an important indicator that shows that policyholders are facing difficulties in meeting premium payments is the level of outstanding premiums. Latest data indicates that this is already on the rise. Given the likely outlook of the industry, closer monitoring of companies will continue.

For the Record

BEWARE OF SCAMS - ADVANCE FEE FRAUD & LOTTERY SCAMS

Statement by the Director Financial Intelligence Unit, Reserve Bank of Fiji, 7 May 2007

Members of the public are advised to exercise extreme caution when receiving unsolicited fax, letters or emails providing attractive opportunities to get rich fast with minimal effort. This is most often a common type of fraud known as **Advance Fee Fraud**.

There has been an increase in the number of Fiji citizens who have been defrauded into sending money to foreign nationals as advance fees for **fraudulent business proposals** and **illegal lotteries**.

What is Advance Fee Fraud?

This is a type of fraud where the perpetrators lure their victims by promising them huge sums of money in exchange for assisting the perpetrators in transferring millions of dollars out of a particular country such as Nigeria, Ghana, the Ivory Coast, South Africa, United Kingdom, the Netherlands, Spain, Canada, the United State and Russia. However, victims will be instructed to pay upfront certain fees and charges to enable the transfer of funds to proceed any further.

In other varieties of “advance fee fraud”, victims may be informed that they have won millions of dollars in an overseas lottery or have been named a beneficiary in a multi-million dollar inheritance. Victims will than be informed that before they can access their winnings or their inherited wealth, they have to first pay some type of fees or charges.

How Does the Advanced Fee Fraud Operate?

1. This is a type of fraud where potential victims will receive an unsolicited fax, email, or letter requesting them to assist in **moving millions of dollars out of a particular country through their bank account**. In return for the victim’s assistance in transferring the funds, the victim will receive an attractive percentage of the total funds in question. In other varieties of Advance fee fraud, the perpetrator may inform a potential victim that he/she has **won a prize in a multimillion dollar lottery in a European country; or is a beneficiary of a multi-million dollar inheritance** which is in a foreign bank account. Some victims maybe informed that a term deposit valued at millions of dollars in their name is maintained in a foreign bank or financial institution.

2. Once a victim responds to the initial invitation, the victim will be requested by the perpetrators to **provide certain personal information** such as their bank account details and will be provided with the details of how and when the funds concerned will be transferred to them.

3. At this point the victim will be informed by the perpetrator that before the funds can be transferred into his or her bank account, the victim is required to **pay some administrative costs** upfront such as fees for tax clearances,

transfer tax or for anti-money laundering certificates. The victim will be given instructions on how to make the advance payment and to whom.

4. Once the advance fee is paid by the victim, the perpetrators will cease all communication with the victim. Any attempts by the victim to contact the perpetrators will be unsuccessful. In most instances the victim may be fooled into making more than one advance payment. Once the perpetrators have obtained whatever funds they can from his or her victim, the perpetrators will stop communicating with the victim.

Advice to Members of the Public

The public is advised to exercise extreme care and caution when receiving such unsolicited letters, faxes and emails.

There is often no way of recovering any money lost by participating in such schemes due to the nature of the fraud. Therefore the public is advised to just ignore such unsolicited correspondences or not to respond to it until you have verified the credentials of the persons involved and you are sure that it is a

genuine proposal.

- **Ignore all unsolicited correspondences** that inform you that you have won a prize in a million dollar lottery. Remember that if you have not purchased a lottery ticket, you cannot win any prize.
- **Do not give out your personal information** such as banking details to complete strangers who establish contact with you through unsolicited correspondences.
- **Do not pay any advance fees** unless you are absolutely sure that the goods and services will be delivered.
- **Discuss first** with your bank, foreign exchange dealer or with the Financial Intelligence Unit before proceeding to make any payment.

If you have participated in such scams and have lost money, there is no avenue for recovering your money due to the nature of the fraud. Do not become a victim, always think sensibly and do not be fooled.

For the Record**WORLD BANK RELEASES ITS REPORT ON FIJI'S FRAMEWORK FOR
COMBATING MONEY LAUNDERING AND TERRORIST FINANCING.**

Statement by the Governor of the Reserve Bank of Fiji, 11 May 2007

The World Bank has recently released its Report on Fiji's framework for combating money laundering and terrorist financing. This Report is the result of an assessment conducted by the World Bank in early 2006 of the measures put in place by Fiji to combat money laundering and terrorist financing. The purpose of the assessment was to determine the extent to which Fiji has implemented the global standards on combating money laundering and terrorist financing.

The Recommendations in the Report

forms an important basis for the Government of Fiji to take us towards full compliance with the international standards and obligations on combating money laundering and terrorist financing.

The full version of the World Bank Report is published on the Reserve Bank of Fiji's website on www.rbf.gov.fj The Report can also be viewed on the Asia Pacific Group on Money Laundering website on www.apgml.org.

For the Record

RESERVE BANK BOARD LEAVES MONETARY POLICY UNCHANGED

Statement by the Governor of the Reserve Bank of Fiji, 29 June 2007

The Reserve Bank Board, at its monthly meeting on 28 June 2007, decided not to make any changes to monetary policy.

In arriving at its decision, the Reserve Bank Governor and Chairman of the Board, Mr. Savenaca Narube said that “We have noted from recent data that the Bank’s current policy mix has been effective in lowering credit growth and slowing imports. Consequently, this has allowed foreign reserves to stabilise in the past few months. Nonetheless, the persisting trade deficit continues to place pressure on our balance of payments.”

The Bank also welcomed the reduction in lending rates announced by some of the commercial banks as the cost of funds had come down significantly in recent months. This easing in interest rates will assist in economic recovery.

In addition, the Governor mentioned that

“inflation picked up sharply in April and May to around 6 percent due largely to a combination of factors. These included supply shortages of domestic market items, Australian drought-related supply disruptions of dairy and wheat products, the impact of the higher fiscal and excise duties announced in March and second round effects of the oil price hikes in recent years. Given these developments, the year-end inflation forecast will likely be revised upwards from the current projection of 3.5 percent. A revised projection should be available in July.” While the sharp increase in inflation in recent months is of some concern but to a large extent this is unavoidable as most of the price increases are beyond our control.

The Bank will continue to closely monitor economic developments over the coming months and fine tune policies as required.

STATISTICAL ANNEX

LIST OF TABLES

I FINANCIAL CONDITIONS	Page No.
1. Reserve Bank of Fiji: Assets	A1
2. Reserve Bank of Fiji: Liabilities	A2
3. Monetary Survey	A4
4. Commercial Banks: Assets	A6
5. Commercial Banks: Liabilities	A8
6. Liquidity Position of Commercial Banks	A10
7. Components of Commercial Banks' Deposits	A12
8. Commercial Banks' Lending and Deposit Rates	A13
9. Commercial Banks' Time Deposit Rates	A14
10. Commercial Banks' Loans and Advances	A16
11. Credit Institutions : Assets	A18
12. Credit Institutions : Liabilities	A20
13. Credit Institutions' Deposit and Lending Rates	A21
14. Credit Institutions' Loans and Advances	A22
15. Money and Capital Market Interest Rates and Yields	A24
16. Fiji Development Bank Loans	A25
17. Fiji National Provident Fund Investments	A26
18. Exchange Rates	A27
19. Key Disclosure Statement : ANZ	A28
20. Key Disclosure Statement : WBC	A29
21. Key Disclosure Statement : BOB	A30
22. Key Disclosure Statement : HBL	A31
23. Key Disclosure Statement : CNB	A32
24. Key Disclosure Statement : MFL	A33
25. Key Disclosure Statement : HFC	A34
26. Key Disclosure Statement : CCFL	A35
II OUTPUT	
27. GDP by Activity at Constant Prices of 1995 (at Factor Cost)	A36
28. Gross Domestic Product	A38
29. Tourist Statistics	A39
30. Visitor Arrivals: By Country of Residence	A40
31. Hotel Statistics	A41
32. Building and Construction	A42
33. Investment	A43
III GOVERNMENT	
34. Government: Expenditure	A44
35. Government: Revenue	A46
36. Government: Summary of Revenue and Expenditure	A47
37. Government: Domestic Debt	A48
38. External Debt	A50

39. Government: Gross Financing	A51
IV PRICES, WAGES AND EMPLOYMENT	
40. Consumer Price Index	A52
41. Wage and Salary Earnings	A53
42. Total Paid Employment	A54
V EXTERNAL	
43. Exports (Merchandise)	A56
44. Imports (Merchandise)	A57
45. Balance of Payments (Accrual Basis)	A58
46. Balance of Payments (Cash Basis)	A60
47. Direction of Trade by Major Trading Partner Countries	A62
VI KEY ECONOMIC AND FINANCIAL INDICATORS	A63

SOURCES:

Reserve Bank of Fiji
Commercial Banks
Fiji Development Bank
Fiji National Provident Fund
Fiji Islands Bureau of Statistics
Ministry of Finance

ABBREVIATIONS

\$: Fiji Dollars unless stated otherwise
m: Million
bn: Billion
(b) Budget
(e): Estimate
(f): Forecast
(p): Provisional
(r): Revised

n.a.: Data not available
n.i.: No issues
n.t.: No trading
-: Zero
RBF: Reserve Bank of Fiji
IMF: International Monetary Fund
CIF: Cost of goods, including insurance and freight to Fiji
FOB: Free on board (the value of goods at Fiji ports before export).